Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, DC 20554

In the Matter of	
Federal-State Joint Board on Universal Service	CC Docket No. 96-45
Schools and Libraries Universal Support Mechanism	CC Docket No. 02-6
Request for Review by Harrisburg City School District of March 3, 2009 Administrator's Decision on Appeal Funding Year 2001-2002	
Form 471 Application Number: 256221 Billed Entity Number: 125727 FCC Reg. Number: 0013480892	

To the Telecommunications Access Policy Division, Wireline Competition Bureau

PETITION FOR RECONSIDERATION OF HARRISBURG CITY SCHOOL DISTRICT

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INTRODUCTION AND SUMMARY

Pursuant to 47 C.F.R. § 1.106, the Harrisburg City School District (the "District") petitions for reconsideration of the December 30, 2016 Order of the Telecommunications Access Policy Division, Wireline Competition Bureau,[1] (the "Division") denying the District's Request for Review of the Universal Service Administrative Company ("USAC")'s decision to order the District to repay more than $2.8 million in E-rate support, and increasing the amount the District would be required to repay up to $5 million. The Division's *Order* failed to address the District's alternative request for a waiver, despite the Commission's previous decision to reserve "discretion to depart from [its] general standards when application would be contrary to the public interest."[2] The facts of this case cry out for a waiver. The District—the victim of a bribery scheme by its E-rate contractor—discovered the scheme, alerted the police, and fully cooperated with USAC's investigation, enabling USAC to make a full claim for restitution from the contractor's owner and criminal mastermind, Ronald Morrett, and the District's former technology director John Weaver. Yet USAC inexplicably failed to inform the U.S. Attorney and the sentencing court of the full amount of money improperly obtained by the criminal conspirators, and thus failed to secure a restitution order covering the full amount of diverted E-rate support—restitution to which USAC was statutorily entitled. Compounding matters further, the Division added to the District's liability all unpaid amounts of restitution, over and above USAC's demand—even though the District has no control over the efforts to collect court-ordered restitution and had no notice that it might be called upon to pay uncollected restitution.

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1 *Request for Review of a Decision of the Universal Serv. Adm'r by Harrisburg City Sch. Dist.; Schs. & Libraries Universal Serv. Support Mechanism*, Order, DA 16-1464, 31 FCC Rcd. 13,549 (Telecomms. Access Policy Div. 2016) ("*Order*").

2 *Schs. & Libraries Universal Serv. Support Mechanism*, FCC 04-190, 19 FCC Rcd. 15,808, 15,815 ¶ 18 n.38 (2004) ("*Fifth Report and Order*").

Imposing a $4 to $5 million liability on a public school district subject to a state-supervised financial recovery plan will cause significant hardship. Here, "special circumstances warrant a deviation from the general rule and such deviation will serve the public interest" better than would strict adherence to the general rule.[3]

The Division should also reconsider its conclusion that the District is responsible for the rules violation, and payment of the underlying funds. The Division's *Order* eschews any analysis of whether John Weaver was acting within the scope of his agency, whether the District adequately supervised Weaver, or whether the harm he caused was reasonably foreseeable—all concepts embodied in common-law principles of negligent supervision, *respondeat superior*, and apparent agency. The Division simply labelled reliance on these venerable principles "misplaced" and imposed liability on the District solely because John Weaver was the District's employee.[4] This strict liability approach is not supported by the *Fourth Report and Order*—which directs recovery based on "responsibility" for a violation, a determination that is inherently fault-based.[5] Strict liability also cannot be supported by the lone Commission decision cited by the Division, *Lazo*, which did not address recovery of support already paid, and would discourage schools from reporting fraud. In any event, if the Commission is going to follow a strict liability approach—of which the District could not possibly have had notice—then the case for a waiver here is even more compelling.

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3 *Ne. Cellular Tel. Co. v. FCC*, 897 F.2d 1164, 1166 (D.C. Cir. 1990).

4 *See* Order ¶ 13.

5 *See Fed.-State Joint Bd. on Universal Serv.; Changes to the Bd. of Dirs. for the Nat'l Exch. Carrier Ass'n, Inc.; Schs. & Libraries Universal Serv. Support Mechanism*, Order on Reconsideration and Fourth Report and Order, FCC 04-181, 19 FCC Rcd. 15,252, 15,256 ¶ 13 (2004) ("*Fourth Report and Order*").

Finally, the Division should reconsider its decision, *sua sponte*, to increase the amount of ordered repayment to include any amounts that were subject to the restitution orders, but which were not collected. By increasing the District's liability without giving it notice or a chance to submit comments in objection, the Division violated the District's due process rights and acted arbitrarily and capriciously. Not once over nearly ten years was the District given notice that it would have to monitor USAC's and the Department of Justice's efforts to collect the court-ordered restitution and serve as the guarantor of their efforts. The Division's decision places an unmanageable burden on a school district and creates the real possibility of double recovery, since the District would be paying amounts that the Department of Justice could still collect from Ronald Morrett and any other surviving defendants.

The Division should put an end to this long saga in the interests of justice: by granting the District's waiver request, or finding that the District is not sufficiently responsible for the violations as to warrant recovery, and in any event limit recovery to the initial amount sought by USAC nearly ten years ago.

FACTS

Harrisburg included a full statement of facts with its Request for Review and incorporates that statement by reference here.[6] The following sets forth a brief summary of the most salient facts. The Harrisburg City School District in Harrisburg, Pennsylvania was and is one of the poorest in the country. The District is currently under a Pennsylvania state-supervised financial recovery plan.[7] In the early 2000s, as part of an earlier financial control effort, the city's mayor

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6 *See* Request for Review of Harrisburg City School District at 4-14, CC Docket Nos. 96-45, 02-6 (filed Apr. 3, 2009) ("Request for Review") (attached as Exhibit 1). For a summary of events, see also the timeline attached as Exhibit 2.

7 *See Harrisburg City Decl. of Fin. Recovery*, Pennsylvania Department of Education (Dec. 3, 2012) http://www.education.pa.gov/Teachers%20-%20Administrators/School%20

made changes to the District's leadership and began a program to improve this disadvantaged school district. As part of this improvement program, the District applied to USAC for E-rate funds to purchase 875 laptop servers for its schools in the 2001-2002 funding year.[8] As envisioned, this technology would allow computers in every classroom to connect to the Internet, with teachers able to control and monitor the students' Internet use.[9]

A. The District Is the Victim of a Major Fraud Scheme.

The District filed its Form 470 in December 2000 and its Form 471 application in January 2001.[10] At the time, the District's director of information technology was John Weaver, a fifteen-year employee. The District also hired a consulting firm, E-Rate Consulting, Inc., to assist it in managing its E-rate process, to advise the District with respect to E-rate compliance, and to complete E-rate applications and related forms. The District listed Weaver as its contact on both Form 470 and Form 471, and Weaver certified the District's Form 470. Although USAC initially denied the Form 471 application, USAC subsequently granted the District's application in February 2002;[11] in April 2002, USAC sent the District, care of Weaver, a Funding Commitment Decision Letter approving $6,150,760 reflecting funding based on a 90 percent discount of the pre-discounted amount of $6,989,500.[12] The service provider for the project was EMO Communications, whose president and owner was Ronald Morrett.

Finances/Pages/Financial-Recovery-for-School-Districts.aspx#tab-1; *Amended Recovery Plan, Harrisburg Sch. Dist., Dauphin Cty. Pa.* (May 31, 2016), http://www.hbgsd.k12.pa.us/UserFiles/Servers/Server_313275/File/School%20Board/Chief%20Recovery%20Officer/Chief%20Recovery%20Officer/Documents/Harrisburg%20SD%20Act%20141%20Amended%20Recovery%20Plan%20FINAL%2005-31-16.pdf.

8 *See* Exhibit 3 at 1 (also appended as Attachment 8 to Request for Review).

9 *See* Exhibit 4 at 1 (also appended as Attachment 9 to Request for Review).

10 Exhibit 5 (also appended as Attachment 5 to Request for Review).

11 *See* Exhibit 6 (also appended as Attachment 6 to Request for Review); Request for Review at 5.

12 *See* Exhibit 7 at 6 (also appended as Attachment 7 to Request for Review).

Unbeknownst to the District, at some time during this period, Ronald Morrett and John Weaver entered into a bribery scheme. From around April 1, 2002 to May 23, 2003, Morrett paid Weaver almost $2 million in bribes in exchange for Weaver falsely certifying that the District had received services from EMO.[13] Morrett sent USAC two falsified invoices stating that EMO had delivered and installed equipment totaling the full $6,150,760 E-rate award.[14] Before paying EMO, USAC required the District to certify that it had actually received the equipment and services listed in the invoices, but, in furtherance of his fraudulent scheme with Morrett, Weaver submitted false certifications to that effect in November 2002 and February 2003.[15] USAC paid both of EMO's invoices.[16] Although the District did eventually receive 787 of the laptops invoiced, EMO never provided the installation, testing, and extended maintenance services it had agreed to, and USAC ultimately concluded that the support paid for these services had been improperly disbursed.

B. Thanks to the District, Weaver and Morrett Are Brought to Justice.

The District eventually discovered this fraud scheme and immediately alerted the police and FBI. The District suspended Weaver, who soon resigned.[17] In December, 2003, after an investigation by the FBI, the Department of Justice charged Weaver and Morrett with theft/bribery under 18 U.S.C. § 666.[18] The District completely cooperated with the Department

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13 *See* Exhibit 8 ¶ 10 (also appended as Attachment 11 to Request for Review).
14 *See* Exhibit 9 (also appended as Attachments 13, 15 to Request for Review).
15 *See* Exhibit 10 (also appended as Attachments 12, 16 to Request for Review).
16 *See* Exhibit 11 (also appended as Attachments 7 and 10 to Attachment 14 to Request for Review).
17 *See* Exhibit 12 (also appended as Attachments 18, 19 to Request for Review).
18 *See* Exhibit 8.

of Justice investigation that led to the criminal charges. In fact, as the District pointed out,[19] a Government press release touted the District's role in bringing Weaver and Morrett to justice.[20]

C. USAC Passes Up Its Opportunity to Receive Full Restitution.

Weaver and Morrett both pleaded guilty. Morrett's plea acknowledged that the Mandatory Victims' Restitution Act of 1996 required "full restitution to all victims for losses those victims have suffered as a result of the defendant's conduct."[21] By the time Weaver and Morrett were sentenced, in the spring of 2005, USAC had already finished an on-site audit, with the District's extensive cooperation. A March 10, 2005 internal memo (nine days after Weaver's sentencing, but two months prior to Morrett's) documented USAC's conclusion that Morrett's company, EMO, had received $5,050,430.95 for ineligible services not provided.[22]

It is significant that USAC knew exactly how much it was owed *before* Morrett was sentenced because, as the District explained in its Request for Review, the Mandatory Victims' Restitution Act of 1996 would have required the sentencing court to award USAC full restitution.[23] Yet despite the fact that USAC knew exactly how much it had been defrauded of at least by March 10—well before Morrett's May 16 sentencing[24]—USAC inexplicably failed to seek full restitution at either sentencing. Instead, on March 30, 2005 (29 days *after* Weaver's sentencing), USAC sent the prosecutor a "Petition for Remission or Mitigation of Forfeiture"

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19 *See* Request for Review at 9.

20 *See* Exhibit 13 (also appended as Attachment 20 to Request for Review).

21 Exhibit 14 at 7 (Plea Agreement of Ronald Morrett) (also appended as Attachment 21 to Request for Review).

22 *See* Exhibit 15 at 4 (also appended as Attachment to Attachment 3 to Request for Review). USAC's audit accounted for the entire $6.15 million.

23 *See* Request for Review at 27 (citing 18 U.S.C. § 3663A *et seq.*).

24 The fact that USAC *completed* its internal memo calculating its damages shortly after Weaver's sentencing strongly suggests that USAC at least knew (or could have known) the amount of damages *before* Weaver was sentenced.

captioned in *Weaver's* case (not Morrett's), declaring that "USAC intends to seek recovery of the balance of the funds not covered by the Court's Judgment . . . from EMO Communications and/or Harrisburg consistent with FCC rules and requirements and any other applicable law."[25] It appears that USAC did not send prosecutors a similar letter concerning Morrett's upcoming sentencing. USAC never filed its restitution "petition" with the court. At Morrett's sentencing, the court inquired about restitution. But because USAC did not inform the court about the amount it lost, the court only ordered restitution in the amount of the bribes EMO paid Weaver: $1,977,516 which Weaver and Morrett owed jointly and severally. Including a third co-conspirator, the total amount of restitution the court ordered was $2,164,956.12, rather than the $5.05 million to which USAC was statutorily entitled.

D. USAC Lets the Case Grow Cold, Then Demands Millions of Dollars from the District.

On September 20, 2007, after more than two years of inaction, USAC sent the District a "Notification of Improperly Disbursed Funds Letter" demanding that the District disburse $2,885,474.96 for "equipment and/or services that were not delivered"—money, of course, that the District never received, because all of the improper funds were paid to EMO.

PROCEDURAL HISTORY

The District appealed USAC's demand. It argued that the assessment was contrary to the facts, and that it violated fundamental principles of agency law providing that an employer is not liable for its employee's crimes carried out outside the scope of the employment. The District also challenged USAC's failure to seek restitution from Morrett, and argued that USAC lacked jurisdiction to pursue its demand. USAC denied the District's appeal on March 2, 2009.

[25] Exhibit 16 at 3 (also appended as Attachment 14 to Petition for Review).

The District filed a Request for Review before the Commission on April 3, 2009. It challenged USAC's holding that the District was "at fault" and therefore liable for recovery, and renewed its argument that USAC's order violates fundamental principles of agency law. It also argued that under the Commission's *Fourth Report and Order* the District was not in the best position to prevent the rule violation that occurred, so it could not be liable for recovery under Commission precedent. Finally, in the alternative, the District requested a waiver of the relevant rules in the event USAC's decision would otherwise be affirmed, based on the hardship to the District and the unique equities of this case.

On December 30, 2016, the Wireline Competition Bureau's Telecommunications Access Policy Division denied the District's appeal.[26] The Division never addressed the District's request for a waiver of repayment. Although the Division acknowledged that there was no evidence anyone at the District other than Weaver was aware of the fraud scheme,[27] the Division affirmed USAC's decision because "[a]t all times relevant to this appeal, Weaver was an official of Harrisburg CSD and was acting in that capacity when he violated program rules."[28] In doing so, the Division acknowledged the District's agency-law arguments, and it admitted that USAC might have erred in holding the District vicariously liable for Weaver's fraud.[29] Nevertheless, the Division failed to address the District's argument that agency law prohibits holding the District liable, because it wrongly believed *Commission* precedent allows for such a result apparently simply because Weaver was a District employee.[30]

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26 *See Order*.
27 *See id.* ¶ 11.
28 *Id.*
29 *Id.* ¶ 13.
30 *Id.*

The Division also *sua sponte* ordered USAC to *increase* the District's potential liability to the *full amount* of improperly released funds, minus the $784,338 in restitution that has been paid to date.[31] The question of whether USAC's demand was *too low* was never presented below, and the Division never suggested that by pursuing its rights to challenge USAC's decision, the District might be exposing itself to even greater liability. Nevertheless, without requesting additional comment, the Division unilaterally increased the District's obligation based on incorrect legal principles.

ARGUMENT

Reconsideration is appropriate here because the Division ignored the District's request for a waiver, and failed to fully address the District's arguments. Because the Division "entirely failed to consider an important aspect of the problem," it was arbitrary and capricious.[32] Moreover, by increasing the District's liability without notice or an opportunity to be heard, the Division's *Order* is based on arguments unknown to the District until the Division's decision.[33]

The Division must consider the District's waiver request. A waiver is more than appropriate when a struggling school district is the victim of a major fraud scheme, but is then told to foot the bill despite USAC's failure to seek full restitution, especially from Morrett, whose company pocketed the illegal fruits of the bribery scheme. The Commission has waived E-rate rules in similar situations, where school districts were involved in rule violations despite their good faith efforts. The Division should also reconsider its decision because the *Order* misapplies established law. The Division misread Commission precedent to conclude that the District is liable, and it failed to conduct the liability analysis the Commission established in its

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31 *Id.* ¶ 14 & n.33.

32 *Motor Vehicle Mfrs. Ass'n of the U.S. v. State Farm Mut. Auto. Ins.*, 463 U.S. 29, 43 (1983).

33 47 C.F.R. § 1.106(b)(2), (c).

Fourth Report and Order. The Division also acted arbitrarily and capriciously and violated the District's due process rights when it *sua sponte* increased the District's potential liability without notice, and without giving the District an opportunity to challenge the legality or fairness of such a ruling.

I. THE EQUITIES STRONGLY SUPPORT A WAIVER, WHICH THE DIVISION DID NOT CONSIDER.

The Division ignored the District's request for a waiver, in the event USAC's decision was affirmed. The District clearly stated that it "respectfully requests . . . that recovery be waived on account of 'hardship, equity, or more effective implementation of overall policy on an individual basis,' pursuant to 47 C.F.R. § 1.3."[34] Yet the Division failed to either acknowledge or rule on the District's waiver request. A waiver is more than justified here.

Waivers are appropriate[35] where strict compliance is inconsistent with the public interest due to special circumstances.[36] In ruling on a waiver, the Commission may consider factors such as hardship, equity, or more effective implementation of overall policy on an individual basis.[37] Indeed, "recovery may not be appropriate for violation of all rules regardless of the reason for their codification."[38] But the Division disregarded the Commission's assurances that "[i]f there are unique reasons why a particular entity believes recovery for a rule violation is inappropriate, that party is always free to present such information in seeking review of USAC's decision,"[39] by

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34 Request for Review at 2. The Commission has recognized that a waiver is appropriate under these circumstances. *See High-Cost Universal Serv. Support; Fed.-State Joint Bd. on Universal Serv.*, Order, FCC 09-16, 24 FCC Rcd. 3369 (2009).

35 A waiver is available and appropriate here because the Division's *Order* made it clear that this case involves a violation of Commission rules. *Order* ¶ 9.

36 *See Ne. Cellular Tel. Co. v. FCC*, 897 F.2d 1164, 1166 (D.C. Cir. 1990).

37 *WAIT Radio v. FCC*, 418 F.2d 1153, 1159 (D.C. Cir. 1969).

38 *Fifth Report and Order* ¶ 19.

39 *Id.* ¶ 29.

ignoring the District's waiver request. The Division should reconsider this request, as it has in the past.[40]

A. Imposing Up to $5 Million in Liability on the District Would Create a Substantial Hardship.

The record shows clearly that saddling the District with a multi-million-dollar recovery obligation would result in tremendous hardship. The District never received one penny of the improperly disbursed funds, so paying USAC back is not a simple matter of disgorging money that is sitting in the District's bank account. Nor can one of the poorest school districts in the nation easily raise millions of dollars. Any recovery USAC received would ultimately be borne on the backs of the District's taxpayers and students.

B. Holding the District Liable Would Undermine the Overall Policy Behind E-Rate.

The Division's decision is contrary to the public interest and greatly impairs the effective implementation of E-rate's overall policy. E-rate is intended to help eligible schools by providing them access to telecommunications services. Imposing strict liability for millions of dollars—dollars that will necessarily be paid by the community the District serves—will not only discourage future school districts from participating in E-rate (to the detriment of their students), but will divert resources that could be better spent on schools within the District, which is more consistent with E-rate's goals.

In the 2004 *Fourth Report and Order*, the Commission declared that E-rate beneficiaries may sometimes be liable for E-rate violations because it wanted to "place sufficient incentive on beneficiaries to ensure compliance"[41] with relevant law. Nothing suggests the Distract lacked a

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[40] *See Request for Review of a Decision of the Universal Serv. Adm'r by Riverside Cty. Office of Educ. Riverside, Cal.; Schs. & Libraries Universal Serv. Support Mechanism*, Order, DA 16-821, 31 FCC Rcd. 7720 (Telecomms. Access Policy Div. 2016) ("*Riverside Order*").

[41] *Fourth Report and Order* ¶ 13.

proper incentive to obey the law—especially considering the district's decision to hire an E-rate compliance consultant, and its swift action after discovering the fraud. USAC argued that the District inadequately supervised Weaver—a finding the Division did not address or affirm—but no "incentive" can prevent fraud if a trusted employee decides to act in bad faith. The Division did not find that the District failed to act with the greatest "accountability and care"[42] that could be expected of an innocent school that learns it has been defrauded. This E-rate violation was not caused by a lack of incentive on the District's part to obey the law, so imposing liability on it will not promote the *Fourth Report and Order*'s purposes.

C. Equity Requires a Waiver.

Equitable considerations also justify a waiver here, because USAC sat on its rights by failing to seek adequate restitution from the court, and failed to pursue recovery from EMO. The Mandatory Victims' Restitution Act *required* the sentencing court to order Weaver and Morrett to pay the *full amount* of restitution needed to cover USAC's losses,[43] but USAC failed to submit timely restitution petitions.

"[E]quity aids the vigilant and not those who slumber on their rights,"[44] where a lack of diligence by one party has prejudiced another party.[45] USAC's failure to pursue its rights in court directly increased the amount of USAC's demand. The Division (and the Commission) should not require the District to bear the financial costs of USAC's decision to sleep on its rights (or its incompetence). USAC also unreasonably delayed demanding recovery from the District, nearly exceeding the five-year limitations period for initiating a recovery action.[46] In

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42 *Id.*

43 *See* 18 U.S.C. § 3663 *et seq.*

44 *Pro-Football, Inc. v. Harjo*, 415 F.3d 44, 47 (D.C. Cir. 2005) (quoting *NAACP v. NAACP Legal Def. & Educ. Fund, Inc.*, 753 F.2d 131 (D.C. Cir. 1985)).

45 *See Pro Football, Inc. v. Harjo*, 565 F.3d 880, 882 (D.C. Cir. 2009).

46 *See* 28 U.S.C. § 2462.

the intervening years, recovery from Morrett and Weaver became more difficult, whereas the District has remained a convenient target. This delay is inexcusable because USAC knew all the relevant facts about this case—including the amount it was owed—back in May 2005 if not earlier.

D. The Commission's Other E-Rate Waivers Justify a Waiver Here.

A waiver here is especially appropriate under the reasoning in the Commission's earlier E-rate waivers. In *Riverside*, the Division found that a school district had violated its E-rate rules by trading in equipment at the wrong fair market value,[47] but found that a waiver was appropriate for several reasons: specifically, the school district acted in good faith, but misunderstood the E-rate rules; the violation took place in the early days of the E-rate program when all parties, including USAC, were less familiar with how E-rate operates; and the district was not attempting to defraud the system.[48]

Like in *Riverside*, there is no suggestion that the District acted in any manner but good faith. It promptly alerted the authorities when it discovered Weaver's fraud, and it participated fully with law enforcement and USAC throughout the entire criminal investigation and prosecution. USAC theorized, but never substantiated its assumption, that the District failed to properly supervise Weaver. Even if that were to be proven, the District should not be punished for holding the good-faith belief that a trusted fifteen-year employee, bound by fiduciary duties to the District, would not commit a federal crime.[49]

Second, like in *Riverside*, this case took place during the early days of E-rate—USAC issued the Funding Commitment Decision Letter in 2002—when all parties were less familiar

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47 *See Riverside Order* ¶ 1.

48 *See id.* ¶ 11.

49 *See id.* ¶ 11 (granting waiver where district "acted in good faith to comply with what it reasonably perceived to be the applicable program rules at the time").

with how the program operated, and the specific ways the program could be defrauded were less foreseeable. Neither USAC nor the District had the benefit of hindsight to inform the level of supervision needed to protect E-rate grants from fraud. Moreover, Weaver's fraud also took place before the Commission had even held that schools could be liable for E-rate violations.[50] The Division relied on the *Fourth Report and Order* to support its affirmance,[51] but it overlooks the fact that that order was not in effect when the District supposedly violated E-rate rules—and thus could not have affected the District's conduct during the time in question here. Even if the 2004 *Fourth Report and Order* technically allows the Commission to impose recovery liability on the District, a waiver is appropriate to avoid subjecting the District to liability under a rule that did not exist at the time of the conduct in question. In 2002, there was also substantially less Commission guidance on the contours of a school's duties to supervise E-rate funding generally. Many of the Commission's decisions regarding early E-rate violations were not released until a decade or more after those violations (and the ones here) took place.[52] A waiver would avoid unfairly subjecting the District to liability for something that occurred before the present body of law on E-rate violations had been developed.

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50 The *Fourth Report and Order* only applied prospectively, to matters for which USAC had not issued a demand letter as of the *Order*'s effective date. *See Fourth Report and Order* ¶ 10. Even though Weaver's fraud took place before the Commission held that schools could be liable for recovery, USAC's long-delayed demand letter was not issued until 2007. This put the District in the worst of two worlds: exposing it to liability for something that happened before the Commission decided schools could face such liability.

51 *See Order* ¶ 10.

52 *See, e.g., Riverside Order* (2016 order applying to 1999 violation); *Coordinated Constr.*, Order, DA 11-1699, 26 FCC Rcd 14,308 (Telecomms. Access Policy Div. 2011) (2011 order applying to 1999 violation); *Idaho Falls Sch. Dist. 91*, Order, DA 10-888, 25 FCC Rcd. 5512 (Wireline Comp. Bur. 2010) (2010 order applying to 1999 violation).

Finally, as in *Riverside*, the District was not attempting to defraud E-rate. Although the Division states that the *District* "falsely certified that services had been delivered,"[53] there is no dispute that the false certification occurred only through the criminal conduct of John Weaver as the agent of Ronald Morrett. Even under the Division's legally unsound theory, no one claims that the District *intended* to defraud the system. In *Riverside*, the Commission granted a waiver when USAC sought to recover the difference between the actual trade-in value of the school district's equipment and the value the district reported. Thus, *Riverside* stands for the proposition that a waiver can be appropriate even when innocent conduct results in an actual loss to the E-rate program. Even if the Commission finds that the District did unknowingly contribute to a loss, the District should receive a waiver because it played a major role in thwarting Weaver's fraud and bringing him to justice, thereby helping secure at least $784,338 of restitution.

Holding an innocent school liable for a fraud it thwarted, for funds it never itself received—especially when USAC failed to secure full restitution from Morrett, the actual criminal mastermind—defies common sense and basic fairness, and is harmful to the public good because it discourages reporting fraud. The Division should reconsider its decision not to grant a waiver here.

II. THE DIVISION IGNORED THE DISTRICT'S AGENCY-LAW ARGUMENTS.

Although the District's Request for Review squarely addressed issue of vicarious liability, refuting USAC's central theory of liability, the Division sidestepped that question altogether. It acknowledged the District's agency-law arguments, and conceded that "USAC

[53] *Order* ¶ 10.

may have incorrectly based its reasoning on vicarious liability."[54] Nevertheless, it concluded that USAC's "end result is correct,"[55] because *Commission* precedent allows E-rate applicants to be held liable for their employees' rule violations.[56] And because the Division believed that Commission precedent allowed USAC to recover from the District, the Division did not actually consider the District's substantive arguments, even though the District argued that "[t]he agency issues in the instant dispute are governed by common-law agency principles . . . ."[57]

The Division should re-consider its decision and apply common-law principles of agency and fault.

A. *Lazo* Does Not Permit the Division to Sidestep the District's Central Argument that the District Cannot Be Held Vicariously Liable for Weaver's Criminal Conduct.

The Division's contention that the District is liable to USAC under the Commission's decision in *Lazo* is wrong.[58] The Division misread that decision, extending it far beyond its facts. In *Lazo*, the Commission affirmed USAC's decision to *deny future payment* on a funding request because a bribery scheme between a school district's employee and lead contractor had tainted the entire contract.[59] In that case, the funds at issue had not been disbursed. Thus, *Lazo* did not involve, and the Commission did not consider, whether agency law and vicarious liability are inapplicable to an effort to claw back funds already disbursed. The decision not to fund a contract in the first instance because it is infected by fraud is fundamentally different from

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54 *Order* ¶ 13.
55 *Id.*
56 *Id.*
57 Request for Review at 17 n.44 (citing *Cmty. for Creative Non-Violence v. Reid*, 490 U.S. 730, 740 (1989)).
58 *Petition for Reconsideration of a Decision of the Wireline Comp. Bur. by Lazo Techs., Inc.*, Order on Reconsideration, FCC 11-177, 26 FCC Rcd 16,663 (2011).
59 *Id.* ¶ 2.

holding every party to the contract liable for repayment after the fact, regardless of its involvement.

The *Order* strips *Lazo* from its context and mistakenly relies on the Commission's holding that the *Lazo* petitioners' "alleged lack of knowledge or involvement in the misconduct . . . is not relevant to whether USAC correctly denied funding for work performed . . . ."[60] The Commission's conclusion in *Lazo* was that when USAC correctly determines not to fund a contract that was procured through fraud, innocent contractors cannot demand E-rate payment simply because they were unaware of the fraud. But the Commission did not hold that those contractors were *liable* for the fraud, or address whether the school district was liable for its employee's conduct. It merely held that a contractor's lack of knowledge is not dispositive of whether USAC's decision to withhold funds is proper.[61] The question of when USAC can *deny payment* is fundamentally different from the question of who is liable to repay USAC for improperly disbursed funds. *Lazo* is inapposite.

The sole basis for the Division's affirmance is a misunderstanding of Commission precedent. Because the Division never addressed the District's substantive agency arguments, or even the threshold question of whether common-law principles govern this dispute, the *Order* is left without any legal underpinnings. The Division should reconsider the District's agency-law arguments and reverse USAC's recovery demand.

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60 *Id.* ¶ 6.

61 *Id.* ¶ 8 ("Petitioners' lack of knowledge or involvement in the misconduct is not dispositive of the question of whether Petitioners are entitled to the E-rate funding at issue.").

B. The District Cannot Be Liable for Weaver's Fraud Under Basic Agency-Law Principles.

Under a proper consideration of common-law agency principles, the District cannot be liable to USAC. As the District argued below, an employer is only vicariously liable for the conduct of its employees "acting *within the scope of employment*."[62] The "core issue" is whether the agent "was motivated, in whole or in part, to serve [the principal's] interests."[63] An employee acts outside the scope of his employment when his conduct "occurs within an independent course of conduct not intended by the employee to serve any purpose of the employer."[64] If an employee's conduct "is different in kind from that authorized, far beyond time or space limits, or too little actuated by a purpose to serve the master, then the conduct is not within the scope of employment."[65]

Although there is no suggestion Weaver intended to benefit the District, the Division refused to adhere to these firmly established principles. It concluded that Weaver was "authorized to conduct E-rate business on behalf of [the District]" and while acting in that capacity, he "caused [the District] to violate E-rate program rules."[66] But this is begging the question—Weaver did not cause *the District* to violate E-rate rules, because his kickback scheme was clearly intended to benefit *himself* and only himself. It is undisputed both that the District

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62 Restatement (Third) of Agency § 7.07(1); *id.* § 7.03(2)(a) (emphasis added).

63 *Siemens Building Techs., Inc. v. PNC Fin. Servs. Grp., Inc.*, 226 F. App'x 192, 196 (3d Cir. 2007).

64 Restatement (Third) of Agency § 7.07(2).

65 *Majano v. United States*, 469 F.3d 138, 141 (D.C. Cir. 2006) (citing Restatement (Second) of Agency § 228).

66 *Order* ¶ 13.

was unaware of Weaver's actions,[67] and that they caused the District substantial harm.[68] As the District argued to the Division, a principal cannot be liable for an agent's conduct when it is antagonistic to the principal, as Weaver's was.[69]

If the Division had actually entertained the District's agency-law arguments, it could not have concluded that the District is liable to USAC. But since the *Order* rests solely on a misreading of *Lazo*, it lacks any legally sufficient basis for upholding USAC's decision. The Division should re-consider the District's petition, fully address the operative agency-law rules, and reverse USAC's demand.

III. BY IGNORING FAULT, THE DIVISION FAILED TO APPLY THE GOVERNING STANDARD OF WHICH PARTY WAS MORE ABLE TO PREVENT A RULE VIOLATION.

The *Order*'s reasoning is also incomplete because the Division ignored the *Fourth Report and Order*'s obligation to evaluate a party's fault.[70] By requiring USAC to "consider which party was in a *better position* to prevent the statutory or rule violation, *and* which party committed the act or omission that forms the basis for the statutory or rule violation,"[71] the *Fourth Report and Order* rejected a strict liability, and instead required a determination of who was at fault. Evaluating fault must include examining what the District could foreseeably have done to prevent the fraud. The Division's refusal to consider common-law agency principles and to weigh the parties' respective abilities to prevent this fraud ignores that requirement.

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67 *See id.* ¶ 11 ("[T]he record contains no evidence that other officials at Harrisburg CSD were aware of Weaver's criminal conduct or sanctioned it . . . .").

68 *See* Request for Review at 20 (noting District incurred over $150,000 in expenses related to investigations and forensic support, and had had its E-rate support stopped for over a year).

69 *See Todd v. Skelly*, 120 A.2d 906, 909 (Pa. 1956).

70 *See Fourth Report and Order* ¶ 15.

71 *Id.* (emphasis added).

Instead of examining the District's fault relative to that of EMO, Morrett, and Weaver, the Division simply concluded that the District "also played a significant role in the rule violations."[72] This is essentially strict liability, informed by 20/20 hindsight. If a school can be liable to USAC for improperly disbursed funds based only on facts it learns after the fraud took place, the *Fourth Report and Order* would be a dead letter, because *ex ante* fault, which the *Fourth Report and Order* requires USAC to consider, would become irrelevant.

Under a faithful application of the *Fourth Report and Order*, the Division should have considered the District's ability foreseeably to prevent the fraud. This would require it to consider the fact that Weaver hid his fraud from the District; the fact that the District went as far as to hire a consultant to ensure it complied with USAC's rules; the fact that Morrett and EMO could have easily prevented the rule violation by not committing fraud in the first place; and the fact that this scheme was unforeseeable. Even USAC did not foresee this fraud, because its rules and forms did not—and indeed, still do not—require the countersignatures USAC claims the District should have used. The Division also should have considered agency and *respondeat superior* law which has specifically evolved to address an entity's fault under circumstances like these. Ignoring these principles and imposing liability based on what USAC learns after the fact will make schools strictly liable for conduct they have no way of knowing about. This would turn the *Fourth Report and Order* on its head, because the Commission explicitly recognized that a party often "is not in a position to ensure that all applicable statutory and regulatory requirements have been met," and that "in many instances, a service provider may well be totally

[72] *Order* ¶ 10.

unaware of any violation."[73] The Division should re-evaluate the District's appeal, correctly applying the standard in the *Fourth Report and Order*, and reverse its earlier decision.

IV. IT WAS ARBITRARY AND CAPRICIOUS, AND A DUE PROCESS VIOLATION, FOR THE DIVISION TO *SUA SPONTE* INCREASE THE DISTRICT'S LIABILITY.

The Division should also reconsider its decision to *sua sponte* instruct USAC to recover *additional* restitution from the District. The Division made this decision without providing any notice that it might do so, and without giving the District any opportunity to argue against it. It is a fundamental rule of law that "due process requires that parties receive fair notice before being deprived of property," and that "in the absence of notice . . . an agency may not deprive a party of property by imposing civil or criminal liability."[74] In the context of an adjudication, the Due Process Clause requires an agency to provide private parties adequate notice of the issues that will be resolved.[75] "It is well-established that a party is entitled to know the issues on which decision will turn and to be apprised of the factual material on which the agency relies for decision so that he may rebut it."[76] An agency must also provide a party with a chance to argue against a potential liability: "The Due Process Clause forbids an agency to use evidence in a way that forecloses an opportunity to offer a contrary presentation."[77]

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[73] *Fourth Report and Order* ¶ 12.

[74] *Trinity Broad. of Fla., Inc. v. FCC*, 211 F.3d 618, 628 (D.C. Cir. 2000) (internal modifications and quotation marks omitted); *see also* U.S. Const. amend. V.

[75] *See Wallaesa v. FAA*, 824 F.3d 1071, 1083 (D.C. Cir. 2016) ("The Due Process and the APA require that an agency setting a matter for hearing provide parties with adequate notice of the issues that would be considered, and ultimately resolved, at that hearing.") (quoting *Pub. Serv. Comm'n of Ky. v. FERC*, 397 F.3d 1004, 1012 (D.C. Cir. 2005)).

[76] *Williston Basin Interstate Pipeline Co. v. FERC*, 165 F.3d 54, 63 (D.C. Cir. 1999) (quoting *Bowman Transp., Inc. v. Arkansas-Best Freight Sys., Inc.*, 419 U.S. 281, 288 n.4) (internal modifications and quotation marks omitted).

[77] *Id.*

The Division ignored this law, never putting the District on notice that its appeal might expose it to greater liability, so the District never had a chance to argue against such a result. In order to cure this constitutional violation, the Division should re-consider this decision and allow the District to be heard on why the Division cannot increase its liability.

A. The Division Failed to Justify Its Authority to Increase a USAC Recovery Demand.

The Division ultimately failed to identify the source of its authority for raising the District's recovery obligation, when no party was requesting that result. The *Fourth Report and Order* charges *USAC* with determining, in the first instance, to whom recovery should be directed,[78] and it requires the recipient of a demand letter to pay "repay the recovery amount."[79] Although USAC's recovery demand was based on a fundamentally unsound legal premise regarding the District's *liability*, there is no reason to doubt its decision not to *apportion* full liability to the District. USAC made its demand based on information that was uniquely available to it following on-site audits, and there is no suggestion that USAC's damages calculations are incorrect—just its liability assessment.

Nothing in the *Fourth Report and Order* suggests the Division has the authority to unilaterally second-guess USAC's decision only to seek partial recovery from the District when that question was not presented for review. Although the Division is authorized to review USAC's liability decision *de novo*, it does not follow that it can review aspects of that decision that are not being challenged, or that a recipient's challenge to a demand letter gives the Division authority to order USAC to expand the scope of its demand. Moreover, the Division is assessing these new amounts long after the expiration of the five-year administrative limitations period.[80]

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78 *See Fourth Report and Order* ¶ 15.
79 *Id.* ¶ 16.
80 *See Fifth Report and Order* ¶ 33.

On reconsideration, the Division should adhere to the 2004 *Fourth Report and Order* and not extend its authority.

B. The *Order* Will Create Perverse Incentives in Future Recovery Cases.

Requiring schools to bear the entire burden of recovering E-rate funds will reward USAC for neglecting viable avenues of recovery from more culpable parties. By allowing USAC to ignore its existing restitution orders, and excuse it from collecting directly from Weaver and Morrett, the *Order* prioritizes recovery from the easiest target, not the parties most able to prevent the rule violation in the first place. Not only is this inconsistent with the *Fourth Report and Order*, it is against the public interest, because in E-rate violation cases, schools will always be easier targets than fraudsters who, by their very nature, cover their tracks and can disappear, or who may be unable to pay restitution while incarcerated. Unlike individual criminals, school districts cannot abscond or conceal assets. Often, when USAC is defrauded, the school may be the only identifiable party remaining, and encouraging USAC to collect from schools, regardless of their involvement or respective ability to prevent fraud, will ensure that underprivileged schools will suffer disproportionately from E-rate violations.

Many schools reading the *Order* may simply decide that seeking E-rate funding to improve their students' educations is not worth it. Those schools will understand that no matter how careful they are *ex ante*, if an employee finds a way to dupe them, USAC—with the Commission's blessing—will come after them for the full amount of the fraud. It will not matter how innocent the school was, or how dilatory USAC was. As long as it is easier to collect from a school than other parties to the fraud scheme, schools will pay a heavy price for factors beyond their control. Any rational school weighing the costs and benefits of participating in E-rate could easily conclude that strict liability for millions of dollars is prohibitive. The Division should re-consider a decision that is so potentially damaging to the E-rate program.

CONCLUSION

The Division's *Order* ignores relevant legal principles and fails to fully apply controlling Commission precedent. Moreover, this case calls out for a waiver. The District was the unknowing victim of Ronald Morrett's bribery scheme, it did not itself receive any of Morrett's ill-gotten E-rate support, and it cooperated with USAC and the police to bring Weaver and Morrett to justice and to put USAC in a position to seek the full amount of restitution. Yet because of USAC's negligence, the District is the party to which USAC and the Division have turned for recovery. The Division should reconsider its decision, and either reverse USAC's recovery demand or waive recovery in light of the unique public interest considerations presented.

Respectfully submitted,

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